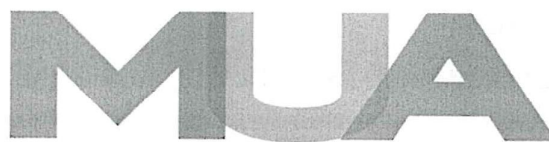


MUA/RASA/EXAM/QP/2014

The
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UNDERGRADUATE UNIVERSITY EXAMINATIONS

SCHOOL OF MANAGEMENT AND LEADERSHIP

DEGREE OF BACHELOR OF MANAGEMENT AND LEADERSHIP/ COMMERCE

BML 301/BCM 224 : FINANCIAL MANAGEMENT

DATE: 2nd DECEMBER 2014

DURATION: 2 HOURS

MAXIMUM MARKS: 70

INSTRUCTIONS:

1. Write your registration number on the answer booklet.
2. **DO NOT** write on this question paper.
3. This paper contains **SIX (6)** questions.
4. Question **ONE** is compulsory.
5. Answer any other **THREE** questions.
6. Question **ONE** carries **25 MARKS** and the rest carry **15 MARKS** each.
7. Write all your answers in the Examination answer booklet provided.

QUESTION ONE

Read the Case Study below carefully and, answer the questions that follow:

Jinowe is a limited company that deals in a variety of business activities in Kenya. The capital structure for the company as at 31/12/2013, is given below:

	Shs.M
Ordinary share capital	
Sh.10 par value	400
Retained earnings	200
10% preference share capital Sh.20 par value	100
12% debenture Sh.100 par value	<u>200</u>
	<u>900</u>

Additional information

1. Corporate tax rate is 30%
2. Preference shares were issued 10 years ago and are still selling at par value MPS = Par value
3. The debenture has a 10 year maturity period. It is currently selling at Sh.90 in the market.
4. Currently the firm has been paying dividend per share of Sh.5. The DPS is expected to grow at 5% p.a. in future. The current MPS is Sh.40.

Required

- a) Determine the WACC of the firm. (10 Marks)
- b) Explain why market values and not book values are used to determine the weights. (5 Marks)
- c) Explain forms of information efficiency in efficient market (5 Marks)
- d) Outline the role of financial institution in Kenyan economy. (5 Marks)

QUESTION TWO

- a) Discuss principles of corporate governance (6 Marks)
- b) Kemco Ltd makes cash payments of Shs.10,000 per week. The interest rate on marketable securities is 12% and every time the company sells marketable securities, it incurs a cost of Shs.20.

Required

- i) Determine the optimal amount of marketable securities to be converted into cash every time the company makes the transfer. (6 Marks)
- ii) Determine the total number of transfers from marketable securities to cash per year. (3 Marks)

QUESTION THREE

Kamwana Limited is considering the purchase of a new machine. Two alternative machines, OTTO and SORD, which will cost Sh.6, 000,000 and Sh.7, 000,000 respectively are available in the market. The cash flow after taxation of each machine are as follows:

Year	Cash flow	
	OTTO	SORD
	Sh.	Sh.
1	600,000	1,800,000
2	1,800,000	2,400,000
3	2,000,000	3,000,000
4	3,000,000	1,800,000
5	2,400,000	1,600,000

Required

- a) Compute:
- i) The net present value of each machine. (8 Marks)
 - ii) Payback period (5 Marks)
- b) Based on the above techniques, advice the company on which machine to buy (2 Marks)

QUESTION FOUR

The following is the balance sheet of KATO Ltd as at 31st December 2002:

	Sh.'000'
Net fixed asset	300
Current assets	<u>100</u>
	<u>400</u>
Financed by:	
Ordinary share capital	100
Retained earnings	70
10% debentures	150
Trade creditors	50
Accrued expenses	<u>30</u>
	<u>400</u>

Additional Information

1. The sales for year 2002 amounted to Sh.500,000. The sales will increase by 15% during year 2003 and 10% during year 2004.
2. The after tax return on sales is 12% which shall be maintained in future.
3. The company's dividend payout ratio is 80%. This will be maintained during forecasting period.
4. Any additional financing from external sources will be affected through the issue of commercial paper by company.

Required

Determine the amount of external finance for 2 years upto 31st December 2004.

(15 marks)

QUESTION FIVE

- a) Discuss three (3) forms of business organization (9 Marks)
- b) Identify the areas of conflict between the management and shareholders of a firm (6 Marks)

QUESTION SIX

- (a) Write short notes on the following
- i. Irredeemable Preference Shares (2 Marks)
 - ii. Management buyout (2 Marks)
 - iii. Efficient portfolios (3 Marks)
- b) Consider two investments, A and B each having the following investment characteristics;

<i>Investment</i>	<i>Expected Return (%)</i>	<i>Proportion</i>
A	10	2/3
B	20	1/3

Required:

- i. Compute the expected return of a portfolio of the two assets. (4 Marks)
- ii. Explain the limitations of capital pricing model (4 Marks)